No. 83-1904

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

BACHE & CO. (LEBANON) S.A.L.,
a Lebanese Corporation,
Petitioner,

v.

ABDALLAH W. TAMARI, LUDWIG W. TAMARI, FARAH TAMARI, co-partners d/b/a WAHBE TAMARI & SONS CO.,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

MOTION OF FUTURES INDUSTRY ASSOCIATION, INC. AND TEN UNITED STATES FUTURES EXCHANGES FOR LEAVE TO FILE BRIEF *AMICI CURIAE*

AND

BRIEF *AMICI CURIAE* IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether the implied private right of action under Section 4b of the Commodity Exchange Act should be expanded to include claims by foreign citizens-residents that their foreign brokerage firms engaged in fraudulent conduct exclusively in a foreign country in connection with the solicitation and operation of a futures trading account.

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MOTION OF FUTURES INDUSTRY ASSOCIATION, INC. AND TEN UNITED STATES FUTURES EXCHANGES FOR LEAVE TO FILE BRIEF *AMICI CURIAE*

The Futures Industry Association ("FIA") and ten United States futures exchanges ("Exchanges")[1] respectfully move, pursuant to Rule 36 of this Court, for leave to file the accompanying brief *amici curiae* in support of the petition for a writ of certiorari to the United States Court of Appeals for the Seventh Circuit, filed on May 21, 1984 by Bache & Co. (Lebanon) S.A.L. The Peti-

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[1] Board of Trade of the City of Chicago; Chicago Mercantile Exchange, Inc.; Chicago Rice & Sugar Exchange; Coffee, Cocoa & Sugar Exchange; Commodity Exchange, Inc.; Kansas City Board of Trade; MidAmerica Commodity Exchange; Minneapolis Grain Exchange; New York Cotton Exchange; and New York Mercantile Exchange.

tioner consented to the filing of the FIA-Exchanges *amici curiae* brief, but the Respondents have refused such consent.

The question presented by the Petition is whether the Seventh Circuit erred in finding that United States courts have jurisdiction to entertain a fraud claim under the Commodity Exchange Act ("CEA") brought by a foreign citizen-resident against his foreign brokerage firm where the alleged misconduct occurred solely in a foreign country in connection with a futures trading account.

The FIA is a not-for-profit corporation whose members are comprised of futures commission merchants ("FCMs"), commercial users of futures markets and others involved in futures trading. Primarily, FIA acts as a principal spokesman on behalf of the multi-billion dollar futures industry. The Exchanges provide a marketplace where futures contracts may lawfully be traded in the United States. *See* Section 4(a) of the CEA, 7 U.S.C. § 6(a) (1982). The Exchanges are charged by statute with important self-regulatory responsibilities relating to the integrity of futures trading. Sections 5 and 5a of the CEA, 7 U.S.C. §§ 7 and 7a (1982).

FIA and the Exchanges represent the great majority of the United States futures business and interests. FIA estimates that over 80 percent of all public trades are effected through FCMs who are FIA members. More than 97 percent of all United States futures contracts are traded through the Exchanges.

As principal spokesmen for and primary components of the United States futures industry, FIA and the Exchanges are obliged to address legal decisions based on errors of law or fact that threaten to have an adverse impact upon futures trading. The Court of Appeals' decision is based on such errors.

The Court of Appeals concluded that the transmission of a customer order by a foreign brokerage firm to the United States constituted substantial conduct within the United States justifying the application of the antifraud provision in Section 4b of the CEA, 7 U.S.C. § 6b (1982), to the foreign firm. Unless reversed by this Court, this decision will reduce liquidity on the United States futures markets, an essential feature of successful futures trading, by chilling foreign market participants who will fear that their foreign customer-broker relationships will be governed by United States laws if they engage in such trading. In addition, this decision could substantially increase the litigation exposure of both FCMs who receive foreign customer orders from foreign brokers and the futures exchanges whose members execute those orders.

FIA and the Exchanges believe that the instant case involves significant issues of public policy involving international commerce generally and futures trading specifically. Moreover, the Court of Appeals' decision was based upon serious misperceptions of law and fact relating to futures trading and the CEA. The Petition of Bache Lebanon, while forceful and compelling, does not fully discuss and emphasize all of these errors and policy considerations.

Therefore, FIA and the Exchanges respectfully move this Court for leave to file their accompanying brief *amici curiae.*

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BRIEF *AMICI CURIAE* OF FUTURES INDUSTRY ASSOCIATION, INC. AND TEN UNITED STATES FUTURES EXCHANGES IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

This brief is submitted on behalf of the Futures Industry Association, Inc. ("FIA") and ten United States futures exchanges ("Exchanges"),[1] as *amici curiae* in support of the petition for a writ of certiorari to the United States Court of Appeals for the Seventh Circuit

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[1] Board of Trade of the City of Chicago; Chicago Mercantile Exchange, Inc.; Chicago Rice & Sugar Exchange; Coffee, Cocoa & Sugar Exchange; Commodity Exchange, Inc.; Kansas City Board of Trade; MidAmerica Commodity Exchange; Minneapolis Grain Exchange; New York Cotton Exchange; and New York Mercantile Exchange.

filed on May 21, 1984 by Bache & Co. (Lebanon) S.A.L. ("Bache Lebanon").

STATEMENT OF INTEREST

FIA is a not-for-profit corporation whose membership includes futures commission merchants ("FCMs"), commercial users of the futures markets and others involved in futures trading.[2] FIA estimates that its FCM members effect more than 80 percent of all futures contracts traded on United States exchanges on behalf of members of the public.

The Exchanges provide a marketplace for the trading of futures contracts in the United States. Futures contracts may lawfully be traded only on exchanges designated by a federal agency, the Commodity Futures Trading Commission ("CFTC"), as contract markets. Sections 4(a), 5 and 6 of the Commodity Exchange Act ("CEA"), 7 U.S.C. §§ 6(a), 7 and 8 (1982). The Exchanges are CFTC-designated contract markets and over 97 percent of all United States futures contracts are traded through the Exchanges.

FIA and the Exchanges oppose the unwise and illogical extension of United States adjudicatory jurisdiction sanctioned by the Court of Appeals (App. B, A-12 - A-13). The Court of Appeals held that a foreign citizen-resident's fraud claim against a foreign brokerage firm, involving alleged misconduct occurring solely in a foreign country, is transformed into a private right of action under Section 4b of the CEA, 7 U.S.C. § 6b (1982), when the foreign firm transmits an order to the United States for a futures contract traded on a domestic exchange (App. B, A-12).

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[2] The important economic benefits of futures trading, the role of FCMs and exchanges, and the basic elements of the regulatory scheme under the Commodity Exchange Act are fully described in Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran, 456 U.S. 353, 357-67 (1982).

1. FIA and the Exchanges have a substantial interest in this controversy. The Court of Appeals' opinion is grounded in numerous misperceptions about futures trading and the CEA that the *amici* have an obligation to correct. Furthermore, by authorizing United States courts to resolve disputes between foreign brokers and foreign customers involving exclusively foreign misconduct, the Court of Appeals' opinion conflicts directly with decisions of this Court and departs from established principles concerning the extraterritorial effect of United States laws.

2. The Court of Appeals' decision will affect adversely the liquidity of United States futures markets by creating a serious, if inadvertent, disincentive for foreign brokers and traders to use domestic markets. In the view of the Court of Appeals, once foreign firms forward foreign customer orders for domestic futures contracts, the relationship between the foreign firm and its foreign customer becomes subject to United States regulatory requirements set forth in the CEA and CFTC Rules.[3] To avoid the complexity and burdens of United States regulation, foreign firms will likely shift their foreign customers' trades from United States to foreign futures exchanges—*e.g.*, exchanges in London, Hong Kong or Japan. As a result, domestic futures market liquidity, which this Court has recognized as vital to successful futures trading, could suffer substantially. *Cf. Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 358-59 (1982).

3. The Court of Appeals' decision also unreasonably enlarges the litigation exposure of the Exchanges and FCMs. For the first time, foreign firms will be required to comply with all applicable CEA and, presumably, exchange requirements. Exchanges may have a correspond-

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[3] In contrast, the CFTC has recently reiterated that foreign brokers are not required to register as FCMs or comply with certain other requirements applicable to FCMs. 49 *Fed. Reg.* 14,721 n.4 (1984).

ing new duty to enforce their self-regulatory rules against nonmember foreign brokerage firms. The Exchanges therefore could be forced to litigate whether foreign customers may bring suits against exchanges for failing to enforce their rules against a foreign broker. *See* Section 22(b) of the CEA, 7 U.S.C. § 25(b) (1982).

Since foreign brokerage firms *must* place orders for United States futures contracts through exchange-member FCMs (Section 4(a) of the CEA, 7 U.S.C. § 6(a)), the jurisdictional nexus defined by the Court of Appeals undoubtedly will also enmesh many FCMs, particularly FCMs with foreign firm affiliates (*see, e.g.*, App. E), in foreign customer fraud suits under Section 4b of the CEA. Indeed, the Second Circuit has recently overturned the dismissal of a foreign customer's Section 4b claim against an FCM for an alleged fraud committed outside the United States by foreign brokers. *Psimenos v. E.F. Hutton & Co.*, 722 F.2d 1041, 1046 (2d Cir. 1983) (transmission of customer orders and trading on United States exchanges through FCMs constituted conduct "substantial enough to establish subject matter jurisdiction").

4. The Court of Appeals' opinion should be reviewed now. Analysis by this Court will serve to establish a unified, consistent judicial framework for determining when, if ever, foreign citizens may resort to United States courts to resolve foreign-based claims.[4] Conflicts

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[4] The Court of Appeals found both the "conduct" and "effects" tests to be satisfied by foreign customer-broker futures fraud (App. B, A-12 - A-13). The Second Circuit upheld jurisdiction solely on a "conduct" theory. *Psimenos v. E.F. Hutton & Co.*, 722 F.2d 1041, 1045 (2d Cir. 1983). The "conduct" and "effects" tests generally emanate from Sections 17 and 18 of the Restatement (Second) of Foreign Relations Law of the United States (1965). Under one formulation, the conduct test looks to whether "significant conduct" occurred in the United States which was an "essential link" in the deception. *Leasco Data Processing Equipment Corp. v. Maxwell*, 468 F.2d 1326, 1334-35 (2d Cir. 1972). The "effects"

among the Circuits on the specific CEA issue raised here are most unlikely. Approximately 98 percent or more of all futures contracts are executed on futures exchanges within the Seventh and Second Circuits. In these Circuits, it is now established that the receipt and execution of futures orders in the United States confers federal court jurisdiction over foreign fraud claims. Prospective foreign customer-plaintiffs therefore can be expected to file suit within either of these Circuits, rather than risk receiving a contrary ruling from another Circuit.

Accordingly, FIA and the Exchanges submit this brief *amici curiae* in support of the instant Petition.

SUMMARY OF ARGUMENT

The private remedy under Section 4b of the CEA established by this Court in *Merrill Lynch* should not apply to completely foreign disputes in the absence of compelling evidence of congressional intent. Under the CEA, the only available evidence indicates Congress did not intend foreign customers to be protected under Section 4b. Moreover, federal court jurisdiction may be invoked only where conduct in the United States constitutes an essential link in the alleged misconduct or has a demonstrably significant impact on important United States interests. The domestic conduct relied upon by the Court of Appeals to sustain United States jurisdiction was not essential, or even related, to the foreign customers' allegations. Rather, transmission of a futures contract order to an exchange-member is an innocuous step in the process of establishing a position in a United States futures contract. In addition, no impact on United States markets occurs if a foreign broker deceives a foreign cus-

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test is satisfied when conduct occurring outside the United States causes foreseeable, direct and substantial effects within the United States. *See Continental Grain (Australia) Pty. Ltd. v. Pacific Oilseeds, Inc.*, 592 F.2d 409, 417 n.12 (8th Cir. 1979).

tomer. While such conduct is not to be condoned, the United States courts need not, and should not, resolve localized, inherently foreign disputes.

ARGUMENT

I. UNDER *MERRILL LYNCH v. CURRAN*, A PRIVATE RIGHT OF ACTION SHOULD NOT BE INFERRED UNDER SECTION 4b OF THE CEA FOR A FOREIGN CUSTOMER AGAINST A FOREIGN FIRM.

In *Merrill Lynch*, this Court authorized futures customers to bring private rights of action for fraud under Section 4b of the CEA, 7 U.S.C. § 6b. This decision was predicated upon two essential elements—(1) routine and consistent judicial recognition of private rights of action under Section 4b prior to 1974; and (2) substantial evidence of congressional intent to perpetuate the preexisting CEA private remedies when Congress amended the CEA in 1974. *Merrill Lynch*, 456 U.S. at 379-88. Specifically, this Court held "the private cause of action under the CEA that was previously available to investors survived the 1974 amendments." *Id.* at 388.

Prior to 1974, no court had permitted a foreign investor to sue a foreign firm under Section 4b of the CEA. Congressional action in 1974 cannot logically be found therefore to have perpetuated a previously unavailable private remedy. By allowing foreign customers to bring Section 4b claims, the Court of Appeals' ruling abridges the explicit limitation on CEA private remedies established in *Merrill Lynch*. Since foreign customers' fraud claims were not part of the "contemporary legal context" in 1974 (*Merrill Lynch*, 456 U.S. at 381), the private remedy enunciated in *Merrill Lynch* should not be drastically expanded to make these claims actionable now in federal court. *Cf. Merrill Lynch*, 456 U.S. at 408 n.17 (Powell, J., dissenting) (permitting an im-

plied right of action "will encourage the discovery of private causes of action of which Congress never dreamed").[5]

To be sure, new implied private rights of action may be inferred where unambiguous evidence exists of congressional intent to create a private remedy. *Merrill Lynch*, 456 U.S. at 378. *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11 (1979). Here the Court of Appeals conceded that there is no "direct evidence" Congress intended Section 4b to apply to a foreign customer's claim against a foreign broker. (App. B, A-10) To the contrary, Congress clearly understands the CEA to cover only "frauds perpetrated on *United States residents* committed by persons located in or outside the United States . . . ." S. Rep. No. 384, 97th Cong., 2d Sess. 109 (1982) (emphasis added).[6] This congressional view reflects the well-settled presumption that Congress does not intend its enactments to cover primarily foreign conduct and disputes. *Foley Brothers, Inc. v. Filardo*, 336 U.S. 281, 284-85 (1949); *Blackmer v.*

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[5] Judicial recognition of an implied private right of action under a particular statutory provision does not render the remedy available to all prospective plaintiffs alleging a violation of that provision. *See, e.g., Santa Fe Industries, Inc. v. Green*, 430 U.S. 462 (1977); *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723 (1975).

[6] In 1982, Congress confirmed that "protection of United States residents" is the sole focus of the CEA's customer protections by expressly authorizing the CFTC, under new Section 4(b) of the CEA, 7 U.S.C. § 6(b) (1982), to proscribe fraud by "those who vend foreign [exchange] futures from domestic locations." H.R. Rep. No. 565, Part 1, 97th Cong., 2d Sess. 52 (1982). Through this enactment, Congress endorsed the central policy underlying the *amici*'s position—the law governing a localized customer-broker fraud claim should be the law of the site of the alleged core misconduct. Moreover, nothing in the language or legislative history of new Section 22 of the CEA, 7 U.S.C. § 25 (1982), even remotely suggests that Congress intended the express private remedy enacted in response to *Merrill Lynch* would be read to extend to a foreign customer's fraud claim against a foreign broker.

United States, 284 U.S. 421, 437 (1932). Accordingly, the Court of Appeals should have rejected the creation of a new federal remedy for foreign futures customers.

II. THE COURT OF APPEALS MISPERCEIVED THE INSIGNIFICANCE OF THE TRANSMISSION TO THE UNITED STATES OF A FUTURES CUSTOMER'S ORDER AND THEREFORE MISAPPLIED THE CONDUCT AND EFFECTS TESTS.

Bache Lebanon allegedly defrauded its customers, the Tamaris, in the opening and management of their futures trading accounts. (App. B, A-5 - A-7) While all the customer-broker contacts and cited misconduct occurred in Lebanon (App. B, A-7), and many of the Tamaris' futures transactions were effected on London exchanges (Pet. at 9 n.8), Bache Lebanon is being subjected to suit in the United States because it performed one customer service—"Bache Lebanon received futures orders from the Tamaris in Lebanon and transmitted them by wire to Bache Delaware for execution" on United States exchanges (App. B, A-6).

The Court of Appeals concluded that providing this customer service satisfied United States subject matter jurisdiction requirements under the "conduct" test (*see supra* n.4) because the transmission of futures customer orders is "an essential step in the consummation of any scheme to defraud through futures trading on United States exchanges." (App. B, A-12) This conclusion is the fundamental flaw in the Court of Appeals' holding.

It is undisputed that Bache Lebanon acted lawfully and properly in forwarding the Tamaris' orders to the United States. Bache Lebanon merely effectuated the Tamaris' instructions by placing their trading orders with an exchange-member FCM. Bache Lebanon, like any other foreign broker whose customer places a United States futures order, had no discretion in this regard; domestic futures contracts must be "executed or consum-

mated by or through" exchange members. Section 4(a)(2) of the CEA, 7 U.S.C. § 6(a)(2) (1982). Thus, Bache Lebanon's innocent and legitimate forwarding of the Tamaris' orders to an exchange-member FCM should not be construed as any part, let alone a significant part, of an illegal scheme.

Bache Lebanon's order transmission was also immaterial in the context of the Tamaris' specific claim. The Tamaris allege that Bache Lebanon fraudulently induced them to open an account and then engaged in deception concerning the operation of the account. Any Bache Lebanon misconduct was consummated in Lebanon. The Tamaris could have asserted that Bache Lebanon committed the same fraudulent acts if it had never transmitted the futures orders, or if all the Tamaris' trades had been executed on London exchanges. The United States contacts and conduct were simply not essential to the Tamaris' allegations.

Ironically, if Bache Lebanon had not forwarded the Tamaris' orders to the United States, it would have engaged in a practice referred to as "bucketing." Bucketing customer orders expressly violates Section 4b(D) of the CEA, 7 U.S.C. § 6b(D) (1982). Under the Court of Appeals' reasoning, however, by bucketing its customers' orders, Bache Lebanon would have escaped the "essential step" in any futures fraud and thereby avoided suit in the United States.[7] Although purporting to promote en-

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[7] *Mormels v. Girofinance, S.A.*, 544 F. Supp. 815 (S.D.N.Y. 1982) demonstrates that the Court of Appeals' presumption that order transmission constitutes an essential step in a futures fraud is in error. In *Mormels*, Judge Weinfeld dismissed a foreign futures fraud claim against a domestic FCM because the alleged misconduct occurred overseas. The fraud scheme in *Mormels* involved United States futures trading to the same nonessential extent as in this case. Futures orders were transmitted and executed in the United States for a foreign customer's account. However, at least ten months after trading had begun for that account, the foreign broker converted his customer's funds. *Id.* at 817. Significantly, in

hanced customer protection, the Court of Appeals' decision thus creates an incentive for a foreign firm engaged in fraud to bucket its customers' orders.

The Court of Appeals would have avoided this inappropriate result by following the basic test that where the "essential core" of an alleged fraud occurs overseas, jurisdiction will not be found in United States courts. *Fidenas v. Compagnie Internationale Pour L'Informatique CII Honeywell Bull, S.A.*, 606 F.2d 5, 8 (2d Cir. 1979). Rather than the core of any misconduct, any Bache Lebanon activities in the United States were "clearly secondary and ancillary." *Id.* at 8. Accordingly, the conduct test was not met here.

The Court of Appeals similarly erred in concluding that jurisdiction should be found under the "effects" test (*supra* n.4). The cited ephemeral and unsubstantiated "effects" on the United States futures markets caused by Bache Lebanon's conduct in Lebanon fall far short of the required level of demonstrable and substantial impact on United States interests. *See, e.g., Schoenbaum v. Firstbrook*, 405 F.2d 200, 206-09 (2d Cir.), *rev'd on other grounds*, 405 F.2d 215 (2d Cir. 1968) (en banc), *cert. denied*, 395 U.S. 906 (1969) (effects test satisfied where foreign misconduct directly impairs value of American investors' stock). The Court of Appeals stated that futures prices and volume "will be artificially influenced" by futures contracts executed on United States exchanges for defrauded foreign customers (App. B, A-12). However, no evidence appears in the record that the Tamaris' futures positions significantly affected the market price. Nor is there any empirical basis for the Court's conclusion that futures contracts entered into as a result of

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Mormels the customer's basic allegations parallelled those of the Tamaris: misrepresentation and mismanagement of a futures account. *Compare, Psimenos*, 722 F.2d at 1047 (distinguishing *Mormels* because "no act which directly caused Mormels' loss occurred in the United States").

fraud inherently have an artificial influence on market price.

Equally unsupportable is the Court of Appeals' concern that public confidence in the markets will be adversely affected unless foreign disputes are adjudicated in the United States. (App. B, A-12) Domestic futures trading will not be harmed if the conduct of a foreign broker in defrauding his customer is required to be addressed under the laws of the country where the fraud occurred. Moreover, the effects test should not be satisfied merely because United States products allegedly were improperly marketed abroad by foreign businessmen. The Court of Appeals' approach, however, could lead to an expansion of federal court jurisdiction to include claims that a foreign automobile salesman deceived a foreign citizen in a foreign country in connection with the sale of a United States manufactured automobile.

By greatly reducing the threshold of domestic conduct and effects required to establish jurisdiction in the United States courts, the Court of Appeals has encouraged foreign citizens to look to the already overworked United States judicial system for resolution of basic foreign customer-broker fraud claims. In addition, the Second and Seventh Circuits have mandated that foreign brokerage firms follow United States laws in dealing with foreign futures customers. As a result, for example, a German citizen-customer who trades United States futures contracts could bring a claim in federal court against a German brokerage firm, which is unaffiliated with any United States firm, alleging that the German firm violated the standards of care established by the CFTC and federal courts under Section 4b of the CEA.[8] Moreover,

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[8] In order to avoid liability for fraud under Section 4b of the CEA, foreign brokers will be required to furnish their foreign customers CFTC-mandated risk disclosure statements and satisfy all other requirements of Section 4b of the CEA. *See* CFTC Rule

domestic FCMs and futures exchanges might also be named as defendants in such an action (*see supra* at 3-4).

The Court of Appeals' decision therefore will cause foreign firms' conduct to be evaluated under United States statutes and in United States courts, rather than under the commercial norms and judicial system of the locale where the firms engage in business. This Court has already rejected the "parochial concept" that the United States can "have trade and commerce in world markets . . . exclusively on our terms, governed by our laws, and resolved in our courts." *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 9 (1972). *See also Piper Aircraft Co. v. Reyno*, 454 U.S. 235, 252, (1981). Thus, review of the Court of Appeals' decision would promote principles of international comity previously established by this Court.

1.55, 17 C.F.R. § 1.55 (1983). Even compliance with CFTC regulations may not be sufficient for foreign brokers since the CFTC has asserted that a broker's disclosure obligations under Section 4b are not necessarily satisfied when a broker provides the CFTC-mandated risk disclosure. 47 *Fed. Reg.* 57,723 (1982).

CONCLUSION

The Court of Appeals' opinion contravenes numerous decisions of this Court, deviates from explicit congressional understanding under the CEA, misconstrues applicable principles governing extraterritorial application of United States law, misperceives fundamental elements of futures trading and regulation under the CEA, expands federal court jurisdiction far beyond the borders ever contemplated by Congress, and compels foreign businesses to comply with United States laws in order to continue to transact futures business for foreign clients. For the foregoing reasons, FIA and the Exchanges, as *amici curiae*, respectfully request that the petition of Bache Lebanon be granted.

Respectfully submitted,

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